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I. G. Mykhalchenko,
PhD in Economics,
Associate Professor of the International
Economics Department,
National Aviation University,
Kyiv, Ukraine
e-mail: i.g.mykhalchenko@gmail.com
ORCID ID 0000-0002-9553-1968

ECONOMIC EFFECTS OF FOREIGN DIRECT INVESTMENT IN HOST-COUNTRY MARKETS

The article examines total (direct, indirect, secondary) economic effects of foreign direct investment and represents theoretical generalization of the principles of influence of TNCs on the host-country markets. An attempt of modeling the impact of direct investment is made. The influence of TNCs on the economic growth of Ukraine is analyzed on the example of TNC «Coca-Cola». Coca-Cola's investment in the local production has contributed to the development of the food sector in Ukraine. Positive trends of foreign direct investment are noted.

Key words: economic effect, foreign direct investment, GDP, host-country markets, market contribution, TNCs.

І. Г. Михальченко. Економічні ефекти прямого іноземного інвестування на ринки приймаючих країн

У глобальних умовах розвитку пряме іноземне інвестування відіграє ключову роль для країн, що розвиваються, оскільки впливає на їх економічний розвиток та структурні реформи. Головними інвесторами на ринку приймаючих країн є транснаціональні корпорації, країнами базування яких є країни високого рівня розвитку. Актуальним вважаємо питання моделювання загального впливу прямого інвестування на секторальні ринки приймаючих країн у цілому.

Метою статті є діагностика безпосередніх та другорядних економічних ефектів прямого інвестування на ринки приймаючих країн.

Методи дослідження включають методи наукового узагальнення, спостереження, синтезу для виявлення ключових факторів впливу прямого іноземного інвестування; статистичні та аналітичні методи узагальнення інформації; моделювання – для встановлення функціональних взаємозв'язків економічних ефектів прямого інвестування ТНК та підвищення у цілому економічного добробуту ринкового приймаючого сектору.

Результати статті полягають у теоретичному узагальненні принципів впливу ТНК на ринки приймаючих країн. Надано спробу розробити модель впливу прямого інвестування на приймаючий ринок з урахуванням прямих та другорядних ефектів. Проаналізовано вплив ТНК на економічне зростання України на прикладі ТНК «Coca-Cola». Інвестиції «Coca-Cola» у місцеве виробництво сприяли розвитку харчового сектору в Україні.

Результати дослідження довели, що пряме інвестування здійснює позитивний вплив від безпосередньої діяльності компанії, підвищує економічне зростання супутніх підприємств на ринку, які виступають її торговельними партнерами та постачальниками. Отже, відбувається зростання всього ринкового сектору, куди направляються інвестиції. ТНК як основні вкладники у розвиваючі ринки приймаючих країн позитивно впливають на її економічний розвиток, підвищуючи рівень ВВП, забезпечуючи робочими місцями, здійснюючи регулярні податкові платежі та підвищуючи доходи громадян, що безпосередньо продемонстровано в результаті аналізу діяльності «Coca-Cola» в Україні.

Ключові слова: ВВП, економічний ефект, приймаючі ринки, прямі іноземні інвестиції, ринковий внесок, ТНК.

The purpose of the article is to detect the direct and secondary economic effects of direct investment in the host-country markets.

Formulation of the problem. The role of foreign direct investment (FDI) is very important in the world. As it's well known, the main investors are transnational corporations (TNCs). It is clear that most countries of TNC origin are highly developed countries. Countries of medium and below average level of economic development are the markets of their activity. Therefore, an important aspect in studying the economic growth of developing countries is the analysis of the economic effects of direct investment in host-country markets.

Analysis of recent research and publications. The difference of economic development of the counties is well studied by lots of scientists, some of them are A. Filipenko, Yu. Makogon, O. Ogor. The role of TNC in the world was analyzed by A. Dunska, M. Pashchenko, E. Avdokushyn, M. Lazgiev, V. Rokocha, V. Melnychuk and others. Such authors as A. Braverman, V. Tomilov, O. Pisotska, V. Zimin, Je. Domasheva, M. Baz' discovered the marketing aspects of investment. However, the issue of modeling the overall impact of direct investment on sectoral host-country markets remains unresolved.

Presentation of basic material of the research. Developing markets take a special place in the system of economic and political relations, have a separate level of economic development and specific features of reproduction and features of socio-economic structure. One of the first and most important feature of developing markets is their place in the world economy and politics. As a part of the world economy, these markets continue to have a tendency of increasing economic and political dependence on the economies of developed markets. Developing markets are major suppliers of raw materials and fuel to the world market. As suppliers of raw materials, they depend on imports of finished products, so today the share of markets in world exports is only about 30 %, including the supply of industrial products – about 20 % [1].

As it was defined by Yu. Makogon, the level of economic development of developing markets can be described as economic backwardness from the most developed part of the world. Low level of development of productive forces, backwardness of technical equipment of industry, agriculture and social infrastructure are the main features of the economy of these markets as a whole. The most characteristic sign of backwardness is the agrarian profile of the economy and the share of the population employed in agriculture [2].

The main task of governments in developing markets is to ensure sustainable economic growth in these countries, as it is the key to socio-economic development. Economic growth is the result of effective public policy and an indicator of the country's well-being and the effectiveness of the country's socio-economic system. And one of the main aspects is to make everything possible to

involve foreign direct investment. The state considers foreign direct investment as an element for creating a competitive economy, ensuring national interests; as an additional source of funding for lack of domestic funds for economic development and difficult access to other sources of funding. Foreign direct investment has a greater impact on the economies of developing markets than developed countries, but this influence is significantly depending on the initial conditions: quality human capital, institutional support, macroeconomic situation in the country. It's very important to balance the interests of the state and foreign investors to achieve maximum effect for both sides of the process.

The key actors determining the scale of FDI in the global economic system are TNCs, which consider the export of capital and its effective placement abroad as the basis for the formation of their economic power. The transfer of a significant part of their production abroad, the creation of branches and subsidiaries there, integrated into a single network of transnational production of goods and services, allows TNCs to use their resources as efficiently as possible, thereby realizing their competitive advantages.

For developing markets, attracting foreign investment is important in the context of structural reforms and economic growth. The main investors are developed countries, which is quite natural from the point of view of Dunning's theory. Therefore, we can summarize that FDI is a real indicator of capital accumulation. Including the benefits of direct investment by TNCs in host-country developing markets, we can summary the main factors that stimulate economic growth (fig. 1).

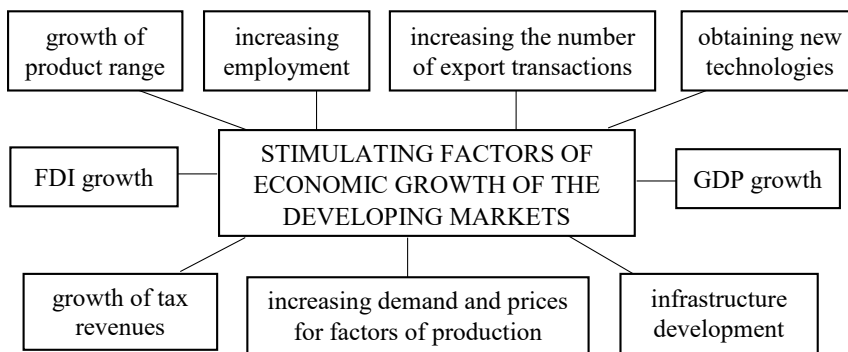


Figure 1. Stimulating factors of economic growth of the developing markets as the result of TNCs activities

Source: formed according to [4, 5, 6].

The estimation of economic effects of TNC activity in developing markets is possible through the calculation of total gross value added, which arises in economy due to the costs of subsidiaries throughout the supply chain and is a contribution to GDP. Gross value added is created directly by subsidiaries companies, its direct suppliers, distributors and outlets. In addition, the economic impact includes the added value associated with consumer demand due to the payment of wages and the redistribution of taxes of subsidiaries and their business partners throughout the economic chain.

At the present stage, there are several approaches to determining the value added. In our study, the components of gross value added of the enterprise include wages, taxes and profits.

This approach is widely used in researches. According to Tchaikovsky, it is expedient at the enterprise not to take into account depreciation as part of gross value added, as it is included in the cost of products (works, services). Thus, value added should be considered as a set of determinants that make up the share of workers, the share of economic entities and the share of the state [6].

The economic impact of TNC's subsidiaries occurs in the results of its activities in the market and forms a mechanism that includes all entities that are directly or indirectly related to the production. This approach involves the assessment of direct and indirect economic effects.

The direct contribution reflects the input to the GDP in the form of remuneration of employees and payment of taxes to the budgets. They include personal income tax and social security contributions, product taxes, other taxes and budget contributions associated with production. In the process of producing goods or services, each enterprise is forced on purchasing raw materials or services from other enterprises, paying wages to employees, making contributions to social funds, paying taxes and, ultimately, making a profit for the owner. Remuneration of employees (including contributions to social funds), taxes and profits form the gross value added created by the enterprise.

The indirect contribution arises as a result of costs for the purchase of goods and services from local suppliers and income of trading partners from selling products. Due to this, local service providers and trading partners receive revenue. The indirect effect of first priority includes the amount of wages, taxes and profits of direct suppliers from the domestic market of the country, distributors and outlets associated with the procurement of company, payments for logistics and margins on the sale of products.

But it should be mentioned the factors of the second and third priorities as they arise as a result that the direct business partners buy goods and services from other companies, and those ones from others. These purchases are not included in the gross value added directly created by the enterprise. However, they form the demand for goods and services of other enterprises. The latter, in turn, respond to demand, make production, pay wages, taxes, make a profit, and purchase goods and services from their counterparties. Their contractors also respond to the description, start production, create added value. Thus, the chain of «demand-production» works in the economy, at each link of which an added amount is created in the remuneration of workers, taxes and profits.

The minor effect arises from the additional demand of households. Employees of the subsidiaries, as well as employees of partners, spend the received payment for work in the consumer market. From this point of view, there were made an attempt of modeling of the market total contribution of TNC activity in the developing market as the main source of FDI in country (fig. 2).

The specificity of this modeling lies in the structural-genetic synthesis of separate surfaces of partners, which play the role of system-forming factors. The indirect effect includes three surfaces of priorities which can directly be expanded.

As a result, there is a multiplier effect – one dollar of value added of the first enterprise creates more than one dollar of value added in the economy as a whole. The magnitude of this effect depends on how deeply the company is integrated into the local economy and how deeply the links with other companies are developed. Purchasing goods from imported suppliers reduces the size of the multiplier effect; the effect will increase as purchases from local producers grow, which in turn depends on the ability of local producers to meet demand. The effect will grow

with the involvement of more contractors from different industries with which the company will cooperate. The share of value added in total production is different for different industries. Links with high value-added industries increase the effect [7].

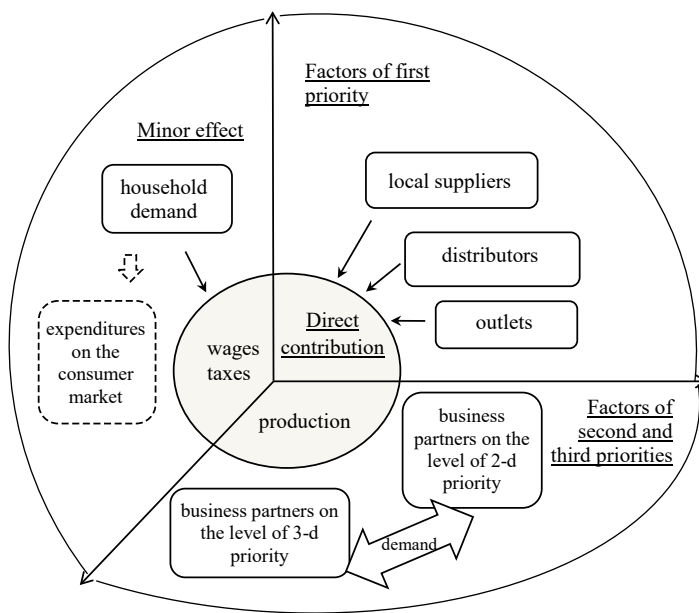


Figure 2. Modeling of total market contribution of FDI

Source: author's approach based on [7, 11].

Thus, the positive aspects for the host-country market of TNCs are the receipt of foreign investment, job creation, the use of technology, the best business experience, and so on. But there are also negatives. That's why the main task is to reconcile the interests of TNCs with the strategic interests of the country's economy. China is a good example. Thanks to the attraction of foreign capital by TNCs, the country received a huge impetus for economic development. The policy of attracting foreign capital in China is still ongoing, and at the beginning of its heyday there were more than 500 of the world's largest corporations. China has managed to combine the interests of TNCs with national interests [8].

Moreover, the inflow of foreign capital has a positive impact on the economic development of Bosnia and Herzegovina (2016) [4] and Romania (2010–2013) [9]. By monitoring and analyzing the various instruments of foreign capital inflow, with an emphasis on investment in the free zone and a joint venture with foreign investors, it has been clearly pointed out the fact that they have diverse, but proven positive impact on macroeconomic variables in the economies.

At the beginning of 2019, there were more than 30 global TNCs in Ukraine, including «Apple», «British Petroleum», «Coca Cola», «Danone», «Hewlett Packard», «Huawei», «McDonalds Corporation», «Metro Cash&Carry», «Microsoft», «Nestle», «PepsiCo», «Procter & Gamble», «Samsung», «Shell», «Toyota», «Unilever», etc. [10]. However, the main attention should be paid to TNCs, which are engaged in the production of products on the territory of Ukraine and, as a consequence, develop the industrial potential of the country and create new jobs.

The most attractive sectors of the economy for foreign TNCs are food and mining industries, agriculture, insurance, finance and trade. One of the conditions for the attractiveness and activity of TNCs is the presence of important factors of production growth: natural resources, cheap and high-quality labor, developed regional transport infrastructure, etc.

«The Coca-Cola Company» is one of the largest multinational corporations in the world, the production of which is also present in Ukrainian market. The company's core sector is consumer goods, the industry is food, the market niche is carbonated beverages. This consumer market giant is a world leader in the production of soft drinks. In Ukraine, the company meets global goals and commitments to sustainable development, updated in 2018, and are represented through subsidiaries of LLC «Coca-Cola Ukraine Limited» and FE «Coca-Cola Beverages Ukraine». In 2019, the products of the System of Coca-Cola Companies in Ukraine were sold in the domestic market of Ukraine, as well as some were exported to Moldova, Armenia and Belarus. Products are sold through three main sales channels:

- modern sales channels – provide direct contact of the consumer with products (chains of supermarkets and hypermarkets, cinemas, gas stations, restaurants, including hotels, cafes, restaurants);
- traditional sales channels – provide for the receipt of products «over the counter» (small offline stores, temporarily built kiosks, as well as small cafes and fast food restaurants);
- wholesale – sales of products in large batches to distributors, not end users.

Traditional and modern sales channels for Coca-Cola Company Systems in Ukraine remain the main in terms of sales. The ratio between the three main sales channels during 2017-2019 remained relatively stable. However, in 2019 there was an increase wholesale due to the reduction of sold beverages for modern sales channels. The largest share of total sales falls on hypermarkets, supermarkets (19.1 %), discounters (10.8 %), retail trade (9.0 %), on the go sales channel (7.7 %), catering establishments and hotels (7.4 %) [7].

Due to the activities of the «System Coca-Cola» companies and cooperation with suppliers and partners in the economy of Ukraine, gross internal product (GDP) is generating, worker places are supporting, labor income is generating and taxes are paying in favor of the state.

The amount of value added amounted to UAH 1 billion in 2020. This is direct contribution to GDP. Factors of first priority amounted to UAH 5.2 billion; second and third priorities – UAH 3.2 billion; minor effect – UAH 1.9 billion. Total contribution in the Ukraine's GDP of the «System of Companies Coca-Cola» in 2020 was UAH 11.3 billion, which corresponds 0.27 % of GDP [11].

The largest share in the structure of total economic influence falls on the indirect effect of the factors of first priority which include direct contribution of clients of the «System of Companies Coca-Cola» in Ukraine from public nutrition sector (UAH 0.5 billion), contribution of suppliers of the Companies in GDP thanks to fulfillment of orders on purchase from the «System Coca-Cola companies» (UAH 1.2 billion), contribution of distributor and retail trading partners, which directly take participation in distribution and sell products of the «Systems of Companies Coca-Cola» in Ukraine (UAH 3.5 billion). 10 UAH of gross value added was created additionally in the economy of Ukraine thanks to each 1 UAH of value added, that was generated by «Coca-Cola» in Ukraine [11].

Such results indicate a high multiplicative influence that ensures the functioning of related sectors of the economy which include wholesale and retail trade, repair of motor vehicles and motorcycles, agriculture, forestry and fisheries, financial and insurance activities, professional,

scientific and technical activities, transport, warehousing, postal and courier activities, information and telecommunications.

Coca-Cola's investments in local production have contributed to the formation of the food industry in Ukraine and the development of the following positive trends over the past 15 years:

1. Reduction of imports of consumer goods.
2. Development of industries related to the food industry, including agriculture, wholesale and retail trade, transport, production of packaging materials.
3. Dissemination of standards of safe, environmentally friendly and resource-efficient production in food industry.
4. Creation of legal and protected jobs.

Thus, the study revealed a positive economic impact of TNC «Coca-Cola: in Ukrainian market, namely the provision of 0.27 % of GDP, 1 % of total investment. Each hryvnia of «Coca-Cola» value added adds UAH 6.9 to Ukraine's GDP, and 18 jobs in related industries are supported by one «Coca-Cola» job.

Conclusions. The impact of FDI on host-country markets is a topical issue and separate views extensively discussed in the literature. This article is an effort to further the understanding of the effects of FDI on economic growth through the activities of TNC on host-country market. Stimulating factors of economic growth of the developing markets as the result of TNCs activities include FDI growth, GDP growth, growth of tax revenues, increasing employment, obtaining new technologies and others.

Economic effects of FDI in host-country markets include direct and indirect contribution in host-country market. Indirect effect consists of factors of first priorities, factors of second and third priorities and minor effect which are represented on the model of total market contribution of FDI.

TNCs, as the main contributors to the development of host-country markets, have a positive impact on its economic development, increasing GDP, providing jobs, making regular tax payments and increasing incomes, as jointly demonstrated by the analysis of «Coca-Cola» activity in Ukraine.

The System of Coca-Cola Companies in Ukraine makes the great contribution to the development of Ukraine's economy. Making foreign direct investment it was contributed UAH 11.3 billion to the GDP of Ukraine; supported domestic business – each hryvnia of added value which was generated by Coca-Cola, created 10 hryvnias in the economy of Ukraine (2020); 18 workplaces in the economy of Ukraine has been supported by one worker place in Coca-Cola.

The further increase of FDI in Ukraine directly depends on the economic situation in the country. The state of affairs in the field of foreign investment currently does not meet the required level of reproduction, which is a kind of marker of investment policy pursued by the country. Today, it is necessary to change tactics and take active measures to attract foreign capital, rather than waiting for a foreign investor to show interest. Only with the effective implementation of economic and administrative reforms, deregulation, measures against corruption, improvement of legislation and law enforcement practices, along with active work to attract foreign investors, the country will be able to become potentially attractive.

Further exploration on this topic is promising because it's necessary to improve institutional basis of FDI in Ukraine, make it more attractive for investment; further research may include the analysis of other sectors of economy where TNC place production.

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И. Михальченко. Экономические эффекты прямых иностранных инвестиций на рынках принимающих стран

В статье исследуются общие (прямые, косвенные, вторичные) экономические эффекты прямых иностранных инвестиций и представлено теоретическое обобщение принципов влияния ТНК на принимающие рынки. Сделана попытка моделирования влияния прямых инвестиций на секторальные рынки. Влияние ТНК на экономический рост Украины анализируется на примере ТНК «Coca-Cola». Инвестиции «Coca-Cola» в местное производство способствовали развитию пищевой промышленности в Украине. Отмечаются положительные тенденции прямых иностранных инвестиций.

Ключевые слова: ВВП, принимающие рынки, прямые иностранные инвестиции, рыночный вклад, ТНК, экономический эффект.

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